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Please bring
forward on

11 20 January

CDP 10/11

Treasury Chambers, Parliament Street, SW1P 3AG

01-233 3000

16 January 1986

Charles Powell Esq
10 Downing Street
LONDON
SW1

Dear Charles,

Signor Craxi wrote to the Prime Minister on 30 December complaining about the exclusion of Italy from G5 Finance Ministers' meetings; the Italian Finance Minister has since written in similar terms to the Chancellor. We have agreed with the FCO that we should let you have a reply for the Prime Minister to send to Signor Craxi. Both the text of the reply (draft attached below) and the suggested timing (see paragraph 4 below) have been agreed with FCO officials.

The Italians (like the Canadians) have complained in the past about their exclusion from G5 meetings and have been similarly rebuffed. While their sense of frustration is understandable - they are the two next largest industrial countries (in terms of GNP) after the G5 - there are good reasons for limiting the G5 to its present membership. The rationale of the G5 grouping is that its members are the major industrial countries whose currencies are internationally held and traded in significant amounts. They therefore have a special interest in and responsibility for the functioning of the currency markets and for the international monetary system. Neither the Italian lira nor the Canadian dollar are of similar importance. (The G5 are also the only Western industrial countries which at present have an Executive Director in the IMF in their own right and whose currencies constitute the SDR).

Enlarging the G5 could not stop at Italy. Canada would certainly insist on joining and it would then become the Summit Seven and it would be difficult to exclude the Commission. This would destroy the informal character and effectiveness of the present grouping. It is very doubtful that the Plaza Agreement could have been negotiated in a G7 meeting. The draft reply therefore makes it clear, politely but firmly, that we expect G5 meetings to continue with their present membership, but that there is no question of the G5 pre-empting decisions which properly belong to other international fora.



It is true, as Signor Craxi claims, that Italy has had to intervene more than any other EC countries in the aftermath of the G5 meeting. But the main reason for this has been the weakness of the lira stemming from lack of confidence in Italian fiscal policy, rather than from any Italian zeal to outdo the G5 countries in driving the dollar down. We have therefore ignored this aspect in the reply.

Tactics and Timing

We have confirmed with other G5 countries, all of whom have also received similar letters from Signor Craxi, that they share our wish not to extend membership to Italy. It is clear, however, that the French and Japanese will wish to put the onus of rebuffing the Italians on the other members of the Group.

The Chancellor is strongly of the view that we should not get out in the lead in sending a negative reply. He therefore recommends that the reply should not be sent until after the G5 meeting. He proposes to discuss the Italian request with his G5 colleagues with a view to an agreement that all five Governments should reply in broadly similar terms as soon as possible after the meetings. As you will see, this outcome is anticipated in the draft reply. The Chancellor would, however, resist any suggestion that we should reply on behalf of the other G5 countries. He also intends to speak to Signor Goria, his Italian counterpart, both before and after the G5 meeting, to keep him in touch with developments. You should therefore hold the draft reply until after the weekend, when we will be in touch with you to let you know whether any amendments need to be made in the light of the meeting.

I am sending a copy of this letter to Len Appleyard (FCO).

Yours Sincerely,

Philip Wynn Owen

P WYNN OWEN
Assistant Private Secretary

DRAFT LETTER

From : The Prime Minister

To : S. Bettino Craxi,
President of the Italian Council of Ministers

Thank you for your letter of 30 December last year about the meeting of the Group of Five Finance Ministers in New York on 22 September and about Italian participation in such meetings. Giovanni Goria has also written to Nigel Lawson on the same subject.

2. I very much welcome the support given in your letter and in the foreign exchange markets to the outcome of the September G5 meeting. I believe that that meeting produced useful results and in particular helped to bring about an overdue adjustment in the value of the dollar to a more realistic level on the foreign exchange markets. This must be beneficial both for the functioning of the international monetary system and for longer-term world economic prospects.

3. As you will know, the Finance Ministers of the Group of Five countries met over the weekend of 18-19 January and Nigel Lawson discussed the question of Italy's participation with his colleagues at that meeting. The other Governments concerned will be replying to you separately. But the comments in the rest of this reply reflect the generally agreed view of all the countries present at the meeting.

4. Informal meetings between the Finance Ministers of the Group of Five have now taken place from time to time over a period of several years. In our view consultations between the five countries, whose currencies are most widely held and traded on the international financial markets, have a natural and useful function in the calendar of international economic meetings. As you may remember, we recognised at the Versailles Economic Summit in 1982 the particular need for multilateral co-operation in respect of the currencies constituting the SDR. I do not believe it would be feasible to widen the participation in these meetings without them losing their specific character and value.

5. The G5 meetings have, as you know, generally been private and deliberative in character. The agreement announced after last September's meeting was exceptional in this respect. That said, I entirely accept that any commitments or conclusions reached at these meetings can apply only to those countries participating in them. I can certainly assure you that, so far as the UK is concerned, there can be no question of the Group of Five meetings seeking to pre-empt or prejudice future decisions which properly belong to any wider international monetary or economic fora. In particular, there can clearly be no question of G5 meetings at Finance Minister level becoming a substitute for the annual Economic Summits, which provide a regular opportunity for the Heads of State

and Government of the leading industrial countries to deal with a much wider spectrum of trade, economic and political issues, as well as with the functioning of the international monetary system.

6. It was agreed at last weekend's discussion that it was essential that the Italian Government should be kept informed at the earliest possible moment about the results of any subsequent Group of Five meetings. As host of last weekend's meeting, Nigel Lawson was in touch with Giovanni Goria before the meeting and [will][has] let him know the results of it.

7. May I take this opportunity to offer you my best wishes for a prosperous and successful New Year?

ECON POL PT2
Exchange Rate

